

## Message Text

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PAGE 01 OTTAWA 02313 252302Z

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ACTION TRSE-00

INFO OCT-01 EUR-25 ISO-00 EB-11 CIAE-00 INR-10 NSAE-00

RSC-01 L-03 FAA-00 MC-02 PM-07 DODE-00 PA-03 PRS-01

USIA-15 COME-00 NSC-10 CIEP-02 OMB-01 DRC-01 /093 W

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FM AMEMBASSY OTTAWA

TO SECSTATE WASHDC 1806

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E.O. 11652: N/A

TAGS: ETRD, EIND, ETRN, US, CA

SUBJECT: CANADIAN OFFSET POLICIES

REF: STATE 178076

1. ECON COUNSELOR MET LAST WEEK WITH ARTHUR (ITC), DURING LATTER'S SHORT STAY IN OTTAWA BETWEEN VISITS TO BOEING AND LOCKHEED, FOR DISCUSSION CANADIAN OFFSET POLICY. ARTHUR SAID THAT ONLY RELEVANT ASPECT OF ISSUE THAT IS FIRM POLICY DECISION IS THAT CANADA SHOULD MAINTAIN AN AEROSPACE INDUSTRY; PRECISELY WHAT THIS INDUSTRY SHOULD LOOK LIKE AND HOW TO ACCOMPLISH THE OBJECTIVE HAS NOT BEEN DECIDED. ARTHUR EMPHASIZED, THEREFORE, THAT HIS COMMENTS REPRESENT PERSONAL VIEWS RATHER THAN ESTABLISHED POLICY. DESPITE THIS DISCLAIMER, WE HAVE IMPRESSION THAT POSITION OUTLINED BY ARTHUR IS THE ONE THAT SENIOR CIVIL SERVANTS HAVE ARTICULATED IN WRITING FOR MINISTERIAL CONSIDERATION AND THAT ITC IS PROCEEDING AS THOUGH POSITION HAD BEEN FORMALLY APPROVED.

2. RE NATURE OF AEROSPACE INDUSTRY, ARTHUR SAID CANADA CANNOT REALISTICALLY HOPE TO BECOME PRIMARY BUILDER OF LARGE AIRCRAFT. LARGE INVESTMENTS REQUIRED AND RISKS LIMITED OFFICIAL USE

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PAGE 02 OTTAWA 02313 252302Z

INVOLVED ARE BEYOND CANADIAN MEANS. CANADA DOES HAVE A

ROLE TO PLAY, AND IS PLAYING IT, IN FIELD OF AIRFRAME COMPONENT ASSEMBLY, ENGINES, AND AVIONICS. IN ARTHUR'S VIEW, PRESENT SIZE OF AEROSPACE INDUSTRY IS ABOUT RIGHT IN TERMS OF INDUSTRY'S CONTRIBUTION TO NATIONAL EMPLOYMENT AND PRODUCTION. FUTURE EMPHASIS SHOULD NOT BE ON EXPANDING OVERALL SIZE BUT RATHER ON SHIFTING INDUSTRY TOWARDS HIGH TECHNOLOGY END OF SPECTRUM.

3. ARTHUR SAID THAT, IN CASES OF LARGE-SCALE PROCUREMENT WHERE GOVERNMENT FUNDS ARE DIRECTLY OR INDIRECTLY INVOLVED, OFFICIALS HAVE OBLIGATION TO ASSESS IMPACT OF TRANSACTIONS ON NATIONAL ECONOMY--NOT ONLY FROM BALANCE OF PAYMENTS STANDPOINT BUT, FOR EXAMPLE, PRODUCTION, EMPLOYEMENT, AND COMPETING CLAIMS ON BUDGETARY RESOURCES--AND ENSURE THAT ECONOMY WILL OBTAIN MAXIMUM BENEFITS IN BROAD SENSE. FORTHCOMING PROCUREMENT OF LRPA (LONG-RANGE PATROL AIRCRAFT) FOR CANADIAN DEFENSE FORCES WHICH MAY COST \$600 MILLION AND AIR CANADA PURCHASE OF BOEING 727'S INVOLVING POSSIBLE COMMITMENT OF \$300 MILLION ARE CASES IN POINT. (LRPA WILL OF COURSE BE FINANCED DIRECTLY FROM BUDGET; AIR CANADA IS GOVERNMENT-OWNED AND GOC IS IN PRACTICE ULTIMATE GUARANTOR OF AIR CANADA'S SOLVENCY.) ARTHUR NOTED THAT SPECIFICATIONS FOR "PHASE I" OF LRPA PROCUREMENT REQUIRED BIDDERS TO INDICATE WHAT THEY WERE PREPARED TO DO TO PROVIDE ECONOMIC BENEFITS TO CANADA. THIS WAS FIRST TIME SUCH A PROVISION WAS WRITTEN INTO SPECIFICATIONS BUT IT WILL PROBABLY BE PATTERN FOR FUTURE MAJOR DEFENSE PROCUREMENTS. AIR CANADA PURCHASE DOES NOT LEND ITSELF TO THIS TYPE OF PRECISE WRITTEN PROVISION BUT ARTHUR MADE NO BONES ABOUT FACT THAT BOEING IS BEING ASKED TO INDICATE WHAT IT CAN DO TO BENEFIT CANADIAN ECONOMY BEFORE COMMITMENT IS APPROVED.

4. ARTHUR SAID POLICY HE DESCRIBED WAS "OFFSET" POLICY ONLY IN VERY LOOSE SENSE. EXPECTED ECONOMIC BENEFITS ARE NOT DEFINED IN TERMS OF FIXED AMOUNT OR PERCENTAGE OF PROCUREMENT, AND THEY NEED NOT BE RELATED DIRECTLY TO TRANSACTION IN QUESTION, I.E. LRPA OFFSET NEED NOT TAKE FORM OF LRPA PARTS PRODUCTION IN CANADA

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PAGE 03 OTTAWA 02313 252302Z

(ALTHOUGH THIS IS OF COURSE NOT EXCLUDED AS POSSIBLE WAY TO MEET OBJECTIVE) BUT MIGHT, FOR EXAMPLE, INVOLVE SETTING UP OF FACILITY IN CANADA FOR R AND D ON AN UNRELATED PROJECT. FURTHERMORE, SATISFACTION OF END-USER REQUIREMENT IS PRIMARY CONSIDERATION AND OFFSET POLICY WILL NOT BE USED TO DISTORT THAT ASPECT OF DECISION-MAKING PROCESS. FINALLY ARTHUR SAID IT WOULD NOT BE HIS INTENTION TO STIMULATE

ESTABLISHMENT OF UNECONOMIC AND NON-COMPETITIVE PRODUCTION FACILITIES IN CANADA. CANADA HAS HAD SUFFICIENT EXPERIENCES WITH THESE (HE MENTIONED CANADAIR'S OPERATIONS AS AN EXAMPLE) AND SHOULD RECOGNIZE THAT THEY CREATE NOTHING BUT PROBLEMS IN LONG-RUN.

5. ARTHUR SAID THAT POTENTIAL U.S. SUPPLIERS (AS WELL AS EUROPEANS WHO CONSIDER THIS STANDARD PROCEDURE) APPEAR TO UNDERSTAND CANADIAN APPROACH AND BE WILLING TO COOPERATE BY, FOR EXAMPLE, MAKING AN EXTRA EFFORT TO OPEN BIDDING ON SUB-CONTACTS TO POTENTIAL CANADIAN SUPPLIERS. BOEING HAD INDICATED TO HIM IN SEATTLE THAT CANADIANS HAVE BID ON AND STAND GOOD CHANCE OF WINNING BIDS FOR SOME SUBCONTRACTS ON NEW 7X7 TRANSPORT. DIALOGUE IS NOT ALL ONE-SIDED, ARTHUR NOTED; U.S. AIRCRAFT MANUFACTURERS HAVE MADE OVERTURES TO CANADIAN GOVERNMENT TO TAKE FINANCIAL INTEREST AND SHARE RISK IN DEVELOPMENT OF NEW AIRCRAFT.

6. IN CONCLUSION, ARTHUR SAID HE HOPED GENERAL POLICY WOULD EVENTUALLY BE FORMALIZED ON PUBLIC RECORD. IN MEANTIME, HE MADE CLEAR HE AND OTHER CONCERNED OFFICIALS INTEND TO CONTINUE EFFORTS ON AD HOC BASIS TO ENCOURAGE ACTIONS BY POTENTIAL SUPPLIERS WHICH WILL CONTRIBUTE TO CANADIAN ECONOMIC GROWTH AND DEVELOPMENT.

7. COMMENT: ARTHUR OBVIOUSLY ATTEMPTED TO PUT BEST FACE ON CANADIAN POLICY AND MAY WELL HAVE DOWNPLAYED EXTENT OF GOC PRESSURE ON POTENTIAL SUPPLIERS. IT IS HARD TO QUARREL WITH IMPLICATION OF HIS OBLIQUE REFERENCE TO EUROPEANS, HOWEVER, THAT IF U.S. SUPPLIERS ARE NOT PREPARED TO PLAY THE GAME OTHERS WILL. ANNOUNCEMENT EXPECTED LATER THIS YEAR OF TWO BIDDERS SELECTED TO LIMITED OFFICIAL USE

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PAGE 04 OTTAWA 02313 252302Z

MOVE INTO "PHASE II" OF LRPA COMPETITION SHOULD PROVIDE INTERESTING EVIDENCE OF HOW OFFSET POLICY ACTUALLY WORKING. (NOTE: RE PARA 4 ABOVE, JETS, PROGRAM BIDS REPORTED OUR A-492 9/24/73 DID REQUIRE 60 PERCENT CANADIAN CONTENT.)  
SCHMIDT

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## Message Attributes

**Automatic Decaptioning:** X  
**Capture Date:** 01 JAN 1994  
**Channel Indicators:** n/a  
**Current Classification:** UNCLASSIFIED  
**Concepts:** CIVIL AVIATION, OFFSET PAYMENTS, AIRCRAFT SALES  
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**Draft Date:** 25 SEP 1973  
**Decaption Date:** 01 JAN 1960  
**Decaption Note:**  
**Disposition Action:** RELEASED  
**Disposition Approved on Date:**  
**Disposition Authority:** garlanwa  
**Disposition Case Number:** n/a  
**Disposition Comment:** 25 YEAR REVIEW  
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**Previous Handling Restrictions:** n/a  
**Reference:** STATE 178076  
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